NO. 57108-1-II

COURT OF APPEALS, DIVISION II
OF THE STATE OF WASHINGTON

LANZCE G. DOUGLASS, INC,

Appellant,

v.

STATE OF WASHINGTON, DEPARTMENT OF REVENUE,

Respondent.

BRIEF OF RESPONDENT

ROBERT W. FERGUSON
Attorney General

Jessica E. Fogel, WSBA No. 36846
Nam D. Nguyen, WSBA No. 47402
Assistant Attorneys General
P.O. Box 40123
Olympia, WA 98504-0123
(360) 753-5515
OID 91027

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases

Statutes

Rules

Regulations

Treatises

I. INTRODUCTION

Lanzce G. Douglass, Inc. (LGD) made a business decision to convey property to an LLC while it constructed homes on the property for eventual sale to third parties. It now seeks to disregard that decision because of its tax consequences. Under Washington tax laws, a construction contractor performing construction services on real property of or for a "consumer" is engaged in a retailing activity. Thus, it must collect and remit retail sales tax, and pay retailing business and occupation (B&O) tax, on the full contract price. *Dep't of Revenue v. Nord Nw. Corp.*, 164 Wn. App. 215, 224-25, 264 P.3d 259 (2011). By contrast, a contractor performing construction services on real property that *it owns* is not engaged in a retailing activity. *Id*. at 225. The former are known as "prime contractors" and the latter as "speculative builders." WAC 458-20-170(1)(a), (2)(a). The difference "turns on whether the person performing the construction owns the real

property on which the construction is performed." *Nord Nw.*, 164 Wn. App. at 225.

Although LGD was not the legal owner of the property when it performed construction services, LGD nonetheless contends that its status as a purchaser under a purchase and sale agreement and other "attributes of ownership" render it the rightful owner entitled to the tax benefits of a speculative builder. These arguments are incorrect as a matter of law.

The purchase and sale agreement did not convey bona fide ownership to LGD, a requirement the Court of Appeals has held is necessary to qualify as a speculative builder. *Nord Nw.*, 164 Wn. App. at 228. Nor can LGD qualify based on the "attributes of ownership" factors listed in the Department rule WAC 458-20-170(2)(a), because they do not create an exception to the ownership requirement. *Nord Nw.*, 164 Wn. App. at 228. Rather, they "are relevant considerations only when necessary to distinguish actual ownership from a mortgage or similar security interest." *Id.* The cases cited by

LGD do not establish otherwise. No evidence suggests that the LLC to which LGD conveyed the property at issue held only a mortgage or security interest in the property.

Absent bona fide ownership of the real property, LGD does not qualify as a speculative builder. This is settled law. *Nord Nw.*, *infra*. The trial court correctly concluded that LGD was engaging in a retailing activity because it did not own the real property. This Court should affirm.

II. RESTATEMENT OF THE ISSUES

Did LGD make retail sales as a prime contractor under RCW 82.04.050(2)(b) when it constructed homes on property owned by a separate LLC?

III. RESTATEMENT OF THE CASE

A. LGD Constructed Homes for Sale on Land Owned by Summerhill LLC

In January 2003, residential home builder LGD acquired a large parcel of land for the purpose of developing residential homes in Spokane, Washington. CP 26. LGD refers to this

parcel as "the Summerhill property." CP 26. LGD acquired the Summerhill property via statutory warranty deed, which was recorded in Spokane County. CP 33.

A short time later, in June 2003, LGD formed a limited liability company, Summerhill LLC, for the purposes of "engaging in the business of owning, developing and managing investments in business and real estate" and "transacting any lawful business . . . in the State of Washington." CP 79-80. LGD was the sole member. *Id*. In July 2004, LGD conveyed its interest in the Summerhill property to Summerhill LLC via quit claim deed, which was recorded in Spokane County. CP 38. Lanzce G. Douglass, owner of LGD (and therefore indirect owner of Summerhill LLC) explained that the reason LGD transferred the property to Summerhill LLC in July 2004 was because he "understood that the arrangement provided some liability protection." CP 29.

The Summerhill property was subdivided into lots and, over the next 10 to 15 years, LGD engaged in construction

activity to improve those lots by building residential homes. CP 28. Between 2014 and 2017, LGD constructed 23 homes on the Summerhill property. CP 30. When LGD completed construction on a home on a particular lot and located a prospective purchaser, LGD would purchase the lot back from Summerhill LLC. CP 28. LGD would then sell the improved lot to a willing homebuyer. *Id.*

This arrangement was set out in a 2004 "Land Form Purchase and Sale Agreement with Earnest Money Provision" (PSA). CP 41. Under the PSA, LGD paid a total of $10 in earnest money in exchange for a commitment from Summerhill LLC to convey the entire Summerhill property, on a lot-by-lot basis at undetermined times in the future, to LGD under specific terms. *See* CP 44 (specifying terms). These terms provided that LGD would have an immediate right of possession, but would not acquire title to the lots until it exercised its right to do so and paid the purchase price of $10 per lot. CP 42, 44. Summerhill LLC would convey the property

to LGD via quit claim deed and then LGD would sell its interest in the property to the homebuyer via statutory warranty deed. CP 58, 61.

Mr. Douglass, owner of LGD, was under the impression that this arrangement, whereby LGD conveyed its interest in the pre-subdivided land to Summerhill LLC prior to construction and then purchased individual subdivided lots from Summerhill LLC after construction, met the requirements for "speculative builder" treatment. CP 29-30. In contrast to "prime contractors" who construct buildings on land owned by others and thus are engaged in retail sales, "speculative builders" construct buildings for sale on land they own. They are not subject to sales tax when they sell the improved real property because they are considered to be selling real estate, not their construction services. RCW 82.04.050(2)(b); WAC 458-20-170(2).

However, because they construct buildings on land they own, speculative builders are the consumers of the materials

and contract labor they purchase and must pay retail sales tax on those purchases. RCW 82.04.190(1)(b); WAC 458-20-170(2)(e); *Riley Pleas, Inc. v. State*, 88 Wn.2d 933, 936, 568 P.2d 780 (1977). Consistent with Mr. Douglass's belief that LGD was a speculative builder, LGD did not collect and remit sales tax on its construction services, but paid sales tax on its purchases of materials and labor. CP 29-30.

B. The Department Audited LGD, Reclassified it as a Prime Contractor, and Issued a Tax Assessment

In December 2017, the Department audited LGD's business activities for the January 2014 through December 2017 audit period. CP 94. During the audit period, LGD had constructed 23 homes on property owned by Summerhill LLC. CP 30. The Department concluded that LGD had erroneously classified itself as a speculative builder with respect to that construction activity because the land was owned by Summerhill LLC, not by LGD, when the construction work was performed. CP 94. The Department reclassified LGD as a prime contractor and issued an assessment for $254,491, comprised of

uncollected retail sales tax, retailing business and occupation tax, interest, and penalties. CP 94, 111.

LGD sought administrative review within the Department, claiming that it had the "attributes of ownership" of the land and, therefore, was a speculative builder under WAC 458-20-170. CP 115. After a hearing, the Department's Administrative Review and Hearings Division issued Determination No. 19-0249, which affirmed the assessment because LGD was not the bona fide owner of the land and therefore, was not a speculative builder. CP 119-20.

Shortly thereafter, LGD paid the assessed amount and filed a de novo refund action in Thurston County Superior Court. CP 1, 6. LGD moved for summary judgment "on the legal issue as to whether it is properly treated as a 'speculative builder' for sales tax purposes." CP 9. LGD argued its "ownership interest under a purchase and sale contract" rendered it a speculative builder and therefore entitled it to a refund of sales and B&O taxes paid. *Id*. In response, the

Department requested the Court grant summary judgment in its favor because LGD did not own the property on which it performed construction activity and thus was not a speculative builder as a matter of law. CP 122. The trial court denied LGD's motion and granted summary judgment to the Department. CP 169. This appeal followed. CP 183.

IV. ARGUMENT

This appeal involves a claim for refund under RCW 82.32.180. That statute places the burden on LGD, as the person seeking the refund, to prove that it overpaid the retail sales tax and retailing B&O tax at issue. *See Avnet, Inc. v. Dep't of Revenue*, 187 Wn.2d 44, 49, 384 P.3d 571 (2016); *Bravern Residential, II, LLC v. Dep't of Revenue*, 183 Wn. App. 769, 776, 334 P.3d 1182 (2014). LGD cannot meet this burden because the undisputed evidence shows that LGD constructed homes on land owned by Summerhill LLC, not on land owned by LGD. The trial court correctly concluded that LGD was not

a speculative builder and was not entitled to the refund it seeks. This Court should affirm.

A. This Court Reviews a Summary Judgment Order De Novo

The trial court denied LGD's tax refund claim on summary judgment. This Court reviews a summary judgment order de novo, engaging in the same inquiry as the trial court. *Activate, Inc. v. Dep't of Revenue*, 150 Wn. App. 807, 812, 209 P.3d 524 (2009). Summary judgment is appropriate when there are no genuine issues of material fact and the moving party is entitled to judgment as a matter of law. CR 56(c).

The trial court granted summary judgment to the Department, as courts may direct summary judgment to the nonmoving party when the material facts are undisputed and the nonmoving party is entitled to judgment as a matter of law. *In re Estate of Toland*, 180 Wn.2d 836, 852-53, 329 P.3d 878 (2014); *see also Impecoven v. Dep't of Revenue*, 120 Wn.2d 357, 365, 841 P.2d 752 (1992); *Hood Canal Sand & Gravel, LLC v. Goldmark*, 195 Wn. App. 284, 295, 381 P.3d 95 (2016)

(recognizing that either party, including a nonmoving party, may receive summary judgment if no material facts are in dispute). The parties agree there were no disputed issues of material fact with respect to LGD's business activities. Thus, this case involves the application of tax statutes and rules to the undisputed facts, which is a question of law this Court reviews de novo. *Wash. Imaging Servs., LLC v. Dep't of Revenue*, 171 Wn.2d 548, 555, 252 P.3d 885 (2011).

B. LGD Made Retail Sales When it Constructed Buildings on Property Owned by Another

Washington imposes a retail sales tax on each retail sale in this state. RCW 82.08.020. In addition, Washington imposes a gross receipts tax on the gross proceeds derived from the business of making retail sales in this state. RCW 82.04.250(1). The term "retail sale" is defined in RCW 82.04.050 and includes services rendered in respect to constructing buildings or other structures upon "real property of or for consumers." RCW 82.04.050(2)(b). The term "consumer" is defined in RCW 82.04.190 and includes "[a]ny person who is an owner,

lessee or has the right of possession to … real property which is being constructed, repaired, decorated, improved, or otherwise altered by a person engaged in business." RCW 82.04.190(4).

Together these provisions dictate that a person performing construction services on real property owned, leased, or possessed by another person is making retail sales. Therefore, the person must pay retailing B&O tax, and must collect and remit retail sales tax, on the gross amount derived from the construction activity. This type of a person is commonly referred to as a "prime contractor." *See* WAC 458-20-170(1)(a). When no selling price is stated, the measure of the taxes is the total amount of construction costs. WAC 458-20-170(3)(b), (4)(a). A prime contractor who fails to collect the retail sales tax from the property owner is personally liable for that tax. RCW 82.08.050(3).

By contrast, a person constructing buildings on real property it owns is not engaged in an activity within the definition of a "retail sale." *Rigby v. State*, 49 Wn.2d 707, 306

P.2d 216 (1957). Such contractors are referred to as "speculative builders." *See* WAC 458-20-170(2)(a). They enjoy certain tax advantages, including that their sales of constructed homes to buyers are exempt from the B&O tax because they are considered to be selling real property. RCW 82.04.390. Thus, they are not subject to B&O tax on the value of their construction services even though the value of the real property is increased. WAC 458-20-170(2)(c). The other tax benefit is that the measure of retail sales tax is lower, since they pay sales tax on the construction materials they purchase and on charges made by their subcontractors, but not on the value of their construction services. WAC 458-20-170(2)(e); *see also Nord Nw.*, 164 Wn. App. at 225 (explaining that speculative builders "receive a tax advantage from the state"). In sum, whether a taxpayer is a prime contractor or a speculative builder makes a difference with respect to what taxes are owed, as the former are making retail sales and the latter are not.

1. LGD was a prime contractor because Summerhill LLC owned the property upon which LGD constructed the homes

As the Court of Appeals has explained, "the distinction between a prime contractor and a speculative builder turns on whether the person performing the construction owns the real property on which the construction is performed." *Nord Nw.*, 164 Wn. App. at 225; *see also Bravern Residential II*, 183 Wn. App. at 779) (member who performed construction services on land owned by separate LLC was not a speculative builder). Summerhill LLC was a separate entity that held legal title to the property upon which LGD constructed the homes. CP 38.

There can be no dispute that the quit claim LGD issued to Summerhill LLC conveyed all of LGD's interest in the property. The deed used the operative words "conveys and quit claims," CP 38, a phrase that Washington courts have long recognized conveys "all the right, title, and interest which the grantor has at the time of making the deed and which is capable of being transferred by deed, unless a contrary intent appears."

Newport Yacht Basin Ass'n of Condo. Owners v. Supreme Nw., Inc., 168 Wn. App. 56, 67, 277 P.3d 18 (2012) (quoting *McCoy v. Lowrie*, 44 Wn.2d 483, 486, 268 P.2d 1003 (1954)). When a deed uses the statutory phrase "conveys and quit claims" as required by RCW 64.04.050, a party cannot use extrinsic evidence to demonstrate an intent to convey less than full title. *Id*.

The quit claim deed here conveyed not only full title to Summerhill LLC, but also "all after acquired title of the grantor(s) therein." CP 38. Courts have held this phrase "negates the possibility that the grantors intended anything but the conveyance of their entire interest in the described property." *Newport Yacht Basin Ass'n*, 168 Wn. App. at 68. Thus, by virtue of the quit claim deed, LGD conveyed all interest it had in the property, and any subsequently acquired interest, to Summerhill LLC.

Nothing more is required to establish that Summerhill LLC was the bona fide owner of the property. Because LGD

performed construction services on Summerhill LLC's land, LGD is not a speculative builder. It was instead a prime contractor engaged in business activities defined as a retail sale under RCW 82.04.050(2)(b). On this basis alone, the Court can and should affirm the trial court's summary judgment order.

2. The Court should not disregard LGD's business decision to transfer the property to Summerhill

LGD transferred the land to Summerhill LLC for a presumably valid business reason. The Court should reject LGD's attempt to walk back that decision because of the tax ramifications. Courts have uniformly rejected the notion that a taxpayer can disregard its business choices in order to change or avoid adverse tax consequences. *Impecoven*, 120 Wn.2d at 364; *Comm'r of Internal Revenue v. Nat. Alfalfa Dehydrating & Milling Co.*, 417 U.S. 134, 149, 94 S. Ct. 2129, 40 L. Ed. 2d 717 (1974) ("This Court has observed repeatedly that, while a taxpayer is free to organize his affairs as he chooses, nevertheless, once having done so, he must accept the tax consequences of his choice, whether contemplated or not, and

may not enjoy the benefit of some other route he might have chosen to follow but did not.") (Citations omitted). *Moline Props. v. Comm'r of Internal Revenue*, 319 U.S. 436, 63 S. Ct. 1132, 87 L. Ed. 1499 (1943) (rejecting corporation's effort to have its corporate existence ignored so that capital gain income could be attributed to its sole shareholder).

LGD seeks to disregard the fact that it conveyed its interests to a separate entity for the benefits that such an arrangement provided, and still take advantage of tax benefits as if it had never made such a conveyance. But Washington courts have repeatedly held that a taxpayer "may not reap the benefits of separate corporate existence (e.g., dispersed corporate liability), and then discard its very own corporate identify when it is advantageous to do so" for tax purposes. *Simpson Inv. Co. v. Dep't of Revenue*, 141 Wn.2d 139, 154, 3 P.3d 741 (2000); *see also Wash. Sav-Mor Oil Co. v. Tax Comm'n*, 58 Wn.2d 518, 521-23, 364 P.2d 440 (1961) (refusing to disregard separateness of parent corporation and wholly

owned subsidiary); *Nord Nw.*, 164 Wn. App. at 229-31 (reversing Board of Tax Appeals ruling ignoring the separateness of a corporation and two LLCs in which it owned an interest). The Court should decline to relieve LGD from the tax consequences of its decision to transfer its ownership interests in the Summerhill property to Summerhill LLC.

3. LGD's status as a purchaser does not render it a bona fide owner

Despite acknowledging that Summerhill LLC held title to the real property at issue, LGD nonetheless seeks treatment as a speculative builder on the grounds that it held a purchaser's interest under the purchase and sale agreement (PSA). Br. Appellant at 15. Specifically, LGD contends that "as the purchaser under a real estate contract, [it] is properly treated as the ***owner*** of the property under state law." *Id*. at 16 (emphasis in original). The Court should reject this argument. The cases on which LGD relies do not stand for the proposition that purchasers under agreements like the PSA are the legal owner of the property prior to closing. Rather, those cases involved a

particular type of "real estate contract," also known as an installment contract, where the sale has closed, but the seller retained title only as a security interest to ensure payment of a loan.

Courts have recognized, as a matter of equity, various rights held by purchasers in installment contracts. For example, in *Tomlinson v. Clarke*, 118 Wn.2d 498, 500, 825 P.2d 706 (1992), the Court held that "purchasers under real estate contracts, like those who purchase real property under other financing devices, may take advantage of the bona fide purchaser doctrine." The bona fide purchaser doctrine recognizes that a good faith purchaser for value, who has no actual or constructive notice of another's interest in the property purchased, has the superior interest in the property. *Id*. The Court extended this doctrine to such buyers, even though the full purchase price remained unpaid and the seller had retained legal title to secure payment, because it perceived no valid reason to distinguish them from buyers who purchase under

other financing devices like mortgages. *Id*. at 503. The *Tomlinson* case establishes only that purchasers who finance through the seller (where the seller retains title as security) have similar rights as those who finance through a mortgage (where a bank holds title as security for repayment of the loan).

Courts have recognized other substantive rights held by purchasers (vendees) in the context of executory "real estate contracts" but these cases do not extend to purchasers under purchase and sale agreements or earnest money agreements. *See Tomlinson*, 118 Wn.2d at 507 (summarizing various rights of vendees). The Court identified the following as examples:

> [A] vendee may contest a suit to quiet title, *Turpen v. Johnson,* 26 Wn.2d 716, 175 P.2d 495 (1946); under the traditional land sale contract, the vendee has the right to possession of the land, the right to control the land, and the right to grow and harvest crops thereon, *State ex rel. Oatey Orchard Co. v. Superior Court,* 154 Wash. 10, 280 P. 350 (1929); . . . a vendee's interest constitutes a mortgageable interest, *Kendrick v. Davis,* 75 Wn.2d 456, 452 P.2d 222 (1969); a vendee is a necessary and proper party for purposes of a condemnation proceeding, *Pierce County v. King,* 47 Wn.2d 328, 287 P.2d 316 (1955) . . .

Tomlinson, 118 Wn.2d at 507 (quoting *Cascade Sec. Bank v. Butler*, 88 Wn.2d 777, 782, 567 P.2d 631 (1977)).

LGD, however, was not a purchaser under the type of "real estate contract" for which courts have recognized such rights. It was a purchaser under a purchase and sale agreement, also known as an earnest money agreement, which constitutes a promise to convey title in the future. *Geonerco, Inc. v. Grand Ridge Props. IV LLC*, 146 Wn. App. 459, 445, 191 P.3d 76 (2008). The primary distinction between "real estate contracts" and earnest money agreements are the means of financing the transaction. William B. Stoebuck & John W. Weaver, *Washington Practice: Real Estate* § 21.4 (2d ed. 2021), CP 139.

"Real estate contracts" are financing devices between a vendor and purchaser, whereas earnest money agreements contemplate that when the deal closes, the parties will make other arrangements to handle the balance of the price. *Id.* The fact that an earnest money agreement may give the purchaser

the right of possession, or impose obligations on the purchaser such as a duty to pay taxes, to insure, or to maintain the premises, does not transform it into a "real estate contract." *Id*.

Here, no evidence suggests that Summerhill LLC financed LGD's purchase of the property and thereby retained only a security interest in the property. The fact that Summerhill LLC would ultimately convey the property to LGD pursuant to the PSA does not render it a "real estate contract" of the type for which courts have recognized the ownership rights of purchasers. Because the PSA is not a true "real estate contract," the cases LGD cites are inapt. LGD cannot rely on them to expand its rights and diminish those of Summerhill LLC. LGD is not a speculative builder because it was not the owner of the property.

This conclusion is consistent with the Supreme Court's holding in *Rigby*, 49 Wn.2d 707, where the Court evaluated an earnest money agreement in deciding that a contractor qualified as a speculative builder. There, the State sought to impose retail

sales tax on construction services the builder provided to purchasers with whom it had entered into earnest money agreements prior to constructing the homes. *Id*. at 710. The builder owned the land during construction, but had entered into earnest money agreements with buyers to sell the improved real property upon completion of the construction activity.

In holding that the builder was not performing construction services for consumers, the Court emphasized that the earnest money agreements "are only the first of a number of instruments comprising the terms of the transactions," which included approval of credits, delivery of mortgages, and delivery of deeds. *Id*. Until the buyers and sellers completed all steps in the sales process, the buyers had no legal "right of possession" to the property as owners and did not otherwise qualify as "consumers" of the construction services. *Id*.

The facts in this appeal amount to the flip-side of *Rigby*. In *Rigby*, the contractor held title to the land but entered into earnest money agreements to convey the land upon completion

of the construction. *Rigby*, 49 Wn.2d at 708-09. Here, the contractor (LGD) did not hold title to the land, but entered into an earnest money agreement allowing it to acquire the land in the future. Thus, unlike the contractor in *Rigby*, LGD was performing construction on someone else's land and its right to obtain legal title and ownership of that land was contingent on completing additional steps in the sale process, which did not occur until LGD completed construction.

Moreover, to the extent that any of these cases support LGD's claim that it had a beneficial interest in the Summerhill property, the Court of Appeals has rejected such an interest as a basis for speculative builder treatment. *Nord Nw.*, 164 Wn. App. at 234 ("even if we assume sufficient evidence [of a beneficial interest in the real property] exists, holding a beneficial interest is not equivalent to ownership under the relevant tax laws."). Thus, whatever "beneficial rights" in the bundle of sticks LGD may have acquired under the earnest money agreement, such rights are insufficient to establish that

LGD was the bona fide owner of the land during construction, as required to obtain the tax benefits of a speculative builder.

4. The "attributes of ownership" in the Department's rule do not create an exception to the bona fide ownership requirement

LGD argues it should be treated as a speculative builder based on its belief that it had sufficient "attributes of ownership" to qualify as a speculative builder under WAC 458-20-170(2)(a). However, proper application of WAC 458-20-170(2)(a) does not support LGD's argument. The rule, WAC 458-20-170(2)(a) ("hereinafter Rule 170(2)(a)"), provides as follows:

> (a) As used herein the term "speculative builder" means one who constructs buildings for sale or rental upon real estate owned by him. The attributes of ownership of real estate for purposes of this rule include but are not limited to the following: (i) The intentions of the parties in the transaction under which the land was acquired; (ii) the person who paid for the land; (iii) the person who paid for improvements to the land; (iv) the manner in which all parties, including financiers, dealt with the land . . . .

The first sentence of Rule 170(2)(a) defines a "speculative builder" as "one who constructs buildings for sale or rental upon real estate owned by him." The second sentence lists four nonexclusive "attributes of ownership."

As the Court of Appeals has explained, the purpose of that second sentence is not to create an exception to the "ownership" requirement in the first sentence, but rather to ensure that any claim of ownership is genuine. *Nord Nw.*, 164 Wn. App. at 227. The rule recognizes that sometimes a formal transfer is not enough to show ownership of real property where the substance of the transaction indicates the real property was transferred for another purpose. *Id*. This conclusion is reinforced by reading Rule 170(2)(a) in context with subsection (2)(b), which provides the following:

> (b) Where an owner of real estate sells it to a builder who constructs, repairs, decorates, or improves new or existing buildings or other structures thereon, and the builder thereafter resells the improved property back to the owner, the builder will not be considered a speculative builder. In such a case that portion of the resale

> attributable to the construction, repairs, decorations, or improvements by the builder, shall not be considered a sale of real estate and shall be fully subject to retailing business and occupation tax and retail sales tax. It is intended by this provision to prevent the avoidance of tax liability on construction labor and services by utilizing the mechanism of real property transfers.

WAC 458-20-170(2)(b) (emphasis added).

This example highlights a scenario when the Department will look beyond the transfer of title in evaluating bona fide property ownership. *Nord Nw.*, 164 Wn. App. at 228. As the Court of Appeals described it, these provisions reflect Washington real property law and the statutory and regulatory scheme that a real property transfer does not always establish property ownership. *Id*. at 227. But the exceptions where a title transfer does not convey bona fide ownership are where the seller or another entity such as a bank or contractor holds title to the property solely as a means of ensuring repayment of a loan. *Id*. at 227-28 (describing need to look beyond the deed to determine whether recipient actually received property interest

or merely a security interest). Thus, the "attributes of ownership factors listed in WAC 458-20-170(2)(a) are relevant considerations only when necessary to distinguish actual ownership from a mortgage or similar security interest." *Id*. at 228.

LGD's contention that Summerhill LLC holds only a security interest has no evidentiary support. LGD conveyed its full and complete interest in the Summerhill property to Summerhill LLC. It did so for the purpose of protecting the property from potential liability and creditors of LGD. CP 29. The intent of the transaction was for Summerhill LLC to own the property, not hold title merely as a financing mechanism. No documents indicate that Summerhill LLC financed LGD's acquisition of the individual lots. Under the PSA, those acquisitions would not take place until LGD completed construction of the home, found a willing buyer, and exercised its right under the PSA to close on each individual lot. Thus, LGD was not a bona fide owner of the property.

The cases upon which LGD relies do not state otherwise. These cases involve various questions of ownership in other contexts, none of which are relevant to whether a builder is the "bona fide owner," and thus a legitimate speculative builder. For example, in *Dunbabin v. Allen Realty Company*, 26 Wn. App. 660, 665, 613 P.2d 570 (1980), the Court held that purchasers were entitled to specific performance under an earnest money agreement. In contrast, no question of specific performance is at issue here. In *Department of Labor and Industries v. Mitchell Brothers Truck Line, Inc.*, 113 Wn. App. 700, 707-09, 54 P.3d 711 (2002), the Court evaluated who owned trucks for purposes of industrial insurance, an inquiry entirely distinct from the speculative builder analysis.

Other cases involved "real estate contracts," which as described above are not at issue here. These include *In re Freeborn*, 94 Wn.2d 336, 340-42, 617 P.2d 424 (1980), which merely recognized that the seller who retained the deed solely as a security interest held a personal property interest, not real

property, and *Bank of New York v. Hooper*, 164 Wn. App. 295, 302-03, 263 P.3d 1263 (2011), which recognized rights of vendees (buyers) under "real estate contracts." In addition, in *Community of Protesting Citizens v. Val Vue Sewer District*, 14 Wn. App. 838, 842, 545 P.2d 42 (1976), the Court recognized that a vendee under a "real estate contract" has the beneficial ownership interest and therefore a right to protest the formation of a sewer district. As discussed above, Summerhill LLC did not hold the title to the property merely as a security interest to secure a mortgage or loan, and thus the PSA was not a "real estate contract" as contemplated by those cases.

Courts' recognition of a beneficial ownership in other contexts likewise have no relevance to this case. For example, in *City of Kennewick v. Benton County*, 131 Wn.2d 768, 770-73, 935 P.2d 606 (1997), the Court held that a stadium in which the City held legal title, but only 49 percent of the beneficial interest, was entitled to the constitutional property tax exemption for property owned by government entities for only

49 percent of its value. But in the context of speculative builders, the Court of Appeals has explicitly rejected the consideration of whether a builder has a beneficial interest. *Nord Nw.*, 164 Wn. App. at 234 ("holding a beneficial interest is not equivalent to ownership under the relevant tax laws").

None of these cases support expanding the scope of ownership beyond that recognized by the Court of Appeals in *Nord Northwest*. Looking beyond the deed is appropriate only when necessary to distinguish between holders of mere security interests. Summerhill LLC held more than a security interest. Therefore, evaluation of the "attributes of ownership" is not appropriate in this case.

5. LGD was not a speculative builder under the "attributes of ownership" factors

The attributes of ownership discussed in Rule 170(2)(a) do not create an exception to the ownership requirement and matter only where a mortgage or security interest is at issue. *Nord Nw.*, 164 Wn. App. at 227-28. But even if the Court were to apply these factors, they weigh in favor of concluding that

Summerhill LLC was the bona fide owner, not LGD. The attributes of ownership consist of four, nonexclusive considerations including the parties' intentions when acquiring the land, who paid for the land and improvements to the land, and the manner in which all parties dealt with the land. WAC 458-20-170(2)(a).

While it is undisputed that LGD paid for the land and the improvements to it, the remaining factors support the conclusion that Summerhill LLC was the bona fide owner. LGD claims that "[i]t was always the intent of the parties that all rights and responsibilities with respect to the Summerhill Property, save legal title, would be held by LGD." Br. Appellant at 30. But LGD formed Summerhill LLC for the purpose of owning real estate, including the Summerhill property, and conveyed its interest in the property to Summerhill LLC to protect itself from potential legal liability. CP 29. There was no purpose of conveying the property to Summerhill LLC other than to have Summerhill LLC own it

while LGD performed the construction services. The parties recorded the quit claim deed, thereby conveying to the public that Summerhill LLC owned the property, not LGD. CP 38. These facts support the conclusion that the parties intended for Summerhill LLC to have ownership of the property during the construction period.

The PSA does not demonstrate otherwise. Rather, it shows only that LGD had a right to possess the property and that in the future, it could obtain ownership by triggering the closing provisions and paying the purchase price of $10. CP 44. Had LGD intended to retain ownership of the property throughout the construction process, there would have been no reason to have conveyed the title to Summerhill LLC.[1]

[1] LGD now claims that it was mistaken regarding the extent of liability protection the LLC offered, CP 29, but regardless of whether that is correct or not, LGD's intent was to obtain such protection by forming the LLC and conveying its interest in the Summerhill property to Summerhill LLC. The parties' intent is the relevant inquiry. WAC 458-20-170(2)(a).

The manner in which third parties dealt with the property likewise supports the conclusion that Summerhill LLC was the bona fide owner. The third-party homebuyers may have ultimately purchased the homes from LGD, but they could only do so after LGD elected to close under the PSA and Summerhill LLC transferred its interest to LGD via recorded quit claim deed. LGD could not sell the homes to third-party buyers without doing so because it lacked the right to do so.

LGD also contends it borrowed funds from U.S. Bank to help fund its general business operations, and provided the Summerhill property as security. Br. Appellant at 32. But the face of the deed of trust indicates that Summerhill LLC was the grantor of this deed of trust. CP 46. Summerhill LLC's representation to the bank that it was the property owner undermines LGD's claim that third parties considered Summerhill LLC to hold merely a security interest. Therefore, even if the attributes of ownership inquiry applies here, the

attributes support the conclusion that Summerhill LLC owned the property.

V. CONCLUSION

LGD performed construction services on property owned by Summerhill LLC. The Department properly assessed retail sales tax and retailing B&O tax on LGD because it performed these services as a prime contractor rather than a speculative builder. The Court should affirm the trial court's summary judgment ruling for the Department.

This document contains 5,956 words, excluding the parts of the document exempted from the word count by RAP 18.17.

RESPECTFULLY SUBMITTED this 10th day of August, 2022.

ROBERT W. FERGUSON
Attorney General

Jessica Fogel

JESSICA E. FOGEL, WSBA No. 36846
NAM D. NGUYEN, WSBA No. 47402
Assistant Attorneys General
Attorneys for Respondent
OID No. 91027

PROOF OF SERVICE

I certify that on August 10, 2022, through my legal assistant, I electronically filed and served this document with the Clerk of the Court using the Washington State Appellate Courts' e-file portal and served a copy of this document via electronic mail, pursuant to agreement, on:

Jason Harn
John Colvin
Colvin + Hallett Law
jcolvin@colvinhallettlaw.com
jharn@colvinhallettlaw.com
ecf@colvinhalletlaw.com

I certify under penalty of perjury under the laws of the State of Washington that the foregoing is true and correct.

DATED this 10th day of August, 2022, at Olympia, WA.

s/Nam Nguyen
Nam Nguyen, Assistant Attorney General

ATTORNEY GENERAL'S OFFICE - REVENUE & FINANCE DIVISION

August 10, 2022 - 11:27 AM

Transmittal Information

Filed with Court:	Court of Appeals Division II
Appellate Court Case Number:	57108-1
Appellate Court Case Title:	Lanzce G. Douglass, Inc., Appellant v. Dept. of Revenue, Respondent
Superior Court Case Number:	20-2-01629-0

The following documents have been uploaded:

- 571081_Briefs_20220810112559D2479613_5208.pdf
  This File Contains:
  Briefs - Respondents
  The Original File Name was DORsResptBrf.pdf

A copy of the uploaded files will be sent to:

- Jharn@colvinhallettlaw.com
- ecf@colvinhalletlaw.com
- jcolvin@colvinhallettlaw.com
- nam.nguyen@atg.wa.gov

Comments:

Brief of Respondent

Sender Name: Kyleen Inman - Email: kyleeni@atg.wa.gov
Filing on Behalf of: Jessica E Fogel - Email: Jessica.fogel@atg.wa.gov (Alternate Email: revolyef@atg.wa.gov)

Address:
PO Box 40123
Olympia, WA, 98504-0123
Phone: (360) 753-5528

Note: The Filing Id is 20220810112559D2479613